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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

November 10, 1993

By Hand

Mr. William F. Caton
Acting Secretary
Federal Communications Commission
1919 M Street, NW
Washington, DC 20554

Re: Implementation of Section 309(j) of the
Communications Act, Competitive Bidding
PP Docket No. 93-253

Dear Mr. Caton:

On behalf of Suite 12 Group ("Suite 12"), enclosed please find an original and nine (9) copies of its Comments filed in the above-referenced proceeding.

Please direct any questions regarding this matter to the undersigned.

Sincerely,



Michael R. Gardner
Charles R. Milkis
Counsel for Suite 12 Group

Enclosures

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Competitive Bidding)
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PP Docket No. 93-253

To the Commission

COMMENTS OF SUITE 12 GROUP

November 10, 1993

The Law Offices of
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SUMMARY

Suite 12 Group ("Suite 12") is an entrepreneurial inventor of a revolutionary wireless cellular technology capable of offering consumers a high quality, cost efficient and competitive alternative to cable television and other multimedia services in the largely fallow 28 GHz spectrum band. The reallocation of the 28 GHz band for the proposed Local Multipoint Distribution Service ("LMDS") is the subject of a pending rulemaking proceeding, in which the Commission has tentatively concluded that Suite 12 should be granted a pioneer's preference for its efforts in developing the CellularVision technology.

Suite 12 is reflective of the type of small business which Congress, through explicit mandate, is requiring the Commission to protect and nurture as competitive participants in the telecommunications explosion taking place in the United States. However, if the Commission is not vigilant and prudent in its implementation of competitive bidding procedures, particularly with regard to the local provision of exciting new LMDS services, Suite 12 and other entrepreneurial inventors and small businesses will be inhibited in their ability to participate in providing competitive services to consumers in the U.S.

Accordingly, if the Commission decides to issue LMDS licenses by competitive bidding, it must, at a minimum, adopt the following specific measures in order to ensure that its auction procedures will fulfill the explicit Congressional intent of promoting small business, preventing the concentration

of licenses, ensuring competition by licensing a wide variety of applicants and supporting the development of new technologies:

- (1) adopt a realistic definition of "small business" to include only companies with annual sales of \$75 million or less;
- (2) exclude incumbent spectrum users in competing services from acquiring controlling interests (i.e., no greater than 49% ownership) in LMDS applicants or licensees; and
- (3) allow for small businesses to pay for the spectrum they secure on an interest-free, installment basis during the life of the license.

Without the inclusion of these minimal safeguards in any competitive bidding process adopted by the Commission for LMDS, Suite 12 and other small businesses will be thwarted in their ability to provide the U.S. public with high quality, low cost spectrum efficient services which can compete directly with cable and other incumbent spectrum users.

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PP Docket No. 93-253

To: The Commission

COMMENTS OF SUITE 12 GROUP

Suite 12 Group ("Suite 12"), by its attorneys, hereby files Comments in response to the above referenced Notice of Proposed Rulemaking ("NPRM"). In the NPRM the Commission seeks comment on whether the proposed Local Multipoint Distribution Service ("LMDS") should be subject to competitive bidding, as well as comments relating to the proposed auction procedures.

As discussed below, Suite 12 believes that if the Commission determines that LMDS licenses should be issued by competitive bidding, the Commission should adopt specific measures to ensure that its auction procedures will be consistent with the explicit Congressional intent of the Omnibus Budget Reconciliation Act of 1993 which requires the Commission to promote small business, prevent the concentration of licenses, ensure effective competition by disseminating licenses among a wide variety of applicants, and support the development of new technologies for the benefit of the public. 47 U.S.C. § 309(j)(3).

I. BACKGROUND

In 1985, Vahak Hovnanian, Shant Hovnanian and Bernard Bossard, the partners of Suite 12, began experimenting in the hope of developing a revolutionary wireless cellular technology capable of offering consumers an array of multimedia services in a high quality yet cost efficient manner in the largely fallow 28 GHz spectrum band. Developing the CellularVision technology through a series of experimental licenses, in 1988 Hye Crest Management, Inc. ("Hye Crest"), an affiliate owned by the Suite 12 partners, filed an application for a commercial license to construct and operate a point-to-point microwave system in the 28 GHz band offering 24 channels of video programming to consumers in the New York area. In January 1991, the Commission granted the Hye Crest request, issuing a five year license to provide service within the New York Primary Metropolitan Statistical Area.¹

In September 1991, Suite 12 filed a Petition for Rulemaking seeking the reallocation of spectrum in the 28 GHz band and the establishment of rules for LMDS based on the CellularVision technology, along with a Petition for Pioneer's Preference. Subsequently, in January 1993, the Commission released a Notice of Proposed Rulemaking which proposed to reallocate the 28 GHz band for LMDS and tentatively concluded that Suite 12 should be awarded a pioneer's preference. See Rulemaking to Amend Part 1 and Part 21 of the

¹ Suite 12's subsequent development of the capability to provide 50 channels of video programming resulted in the modification of the Hye Crest license in 1992.

Commission's Rules to Redesignate the 27.5 - 29.5 GHz Frequency Band and to Establish Rules and Policies for Local Multipoint Distribution Service, ("LMDS NPRM"), 8 FCC Rcd 557 (1993).

In the eight years that have elapsed since entrepreneurs/inventors Vahak Hovnanian, Shant Hovnanian and Bernard Bossard first set out to develop a high quality, cost efficient wireless means of delivering an array of multimedia services to consumers in a largely unused portion of the spectrum, the partners have invested significant time and substantial resources towards the development of the current, revolutionary CellularVision technology. From the initial experiments, to the development of the capability to offer 24 video channels, to the further experiments which led to the ability to offer 50 video channels, to the development of the ability to offer video, voice and data services simultaneously, to the development of two-way, interactive capability, and to current experiments involving educational and medical applications of the technology — the creation of the CellularVision technology, as it exists today, is the product of an ongoing process of research, development and experimentation, requiring substantial expenditures of resources.

Suite 12 is committed to licensing its technology as rapidly as possible in markets across the nation. However, if the Commission adopts competitive bidding for LMDS, it must do so in a prudent fashion that will allow Suite 12 and other small businesses to realistically compete with incumbent cable and telco spectrum users who otherwise could stifle competition with their well-

financed encroachment into the largely fallow 28 GHz spectrum. To advance competition and to ensure opportunities for small businesses like Suite 12, the Commission must at a minimum adopt the following measures:

- (1) adopt a realistic definition of "small business" to include only companies with annual sales of \$75 million or less;
- (2) exclude incumbent spectrum users in competing services from acquiring controlling interests in LMDS applicants or licensees; and
- (3) allow for small businesses to pay for the spectrum they secure on an interest-free, installment basis during the life of the license.

Without such protective measures, small businesses like Suite 12 will not only be effectively prevented from becoming LMDS licensees, Suite 12 also will be inhibited from fully and promptly deploying its high quality, low cost alternative video delivery service to consumers throughout the U.S.

II. ARGUMENT

In the NPRM, the Commission proposes that LMDS licenses be issued pursuant to competitive bidding. See NPRM at para. 152. If the Commission determines that LMDS licenses should be issued by auction, Suite 12 believes, for the reasons discussed below, that certain, specific measures must be taken to ensure compliance with the explicit mandate of Congress.

1. Absent Sufficient Protections, Competitive Bidding will Prevent Small Businesses from Competing with Well-Financed, Larger Corporations.

The Omnibus Budget Reconciliation Act of 1993 ("Budget Act") adds new Section 309(j) to the Communications Act of 1934, authorizing the Commission to use competitive bidding to promote "the development and rapid deployment of new technologies, products, and services for the benefit of the public" as well as promoting "economic opportunity and competition . . . by avoiding excessive concentration of licenses and by disseminating licenses among a wide variety of applicants, including small businesses . . ." See 47 U.S.C. § 309(j)(3). Specifically, the Budget Act provides the Commission the authority to use a competitive bidding scheme when mutually exclusive applications are filed for initial licenses or construction permits which use the radio spectrum for services which will receive subscriber-based compensation or fees.² Although the auction process seeks to add revenue to the Federal Treasury, in designing competitive bidding methodologies and making the required public interest determinations, the Commission is not permitted to take into account expected Federal revenues that would result from competitive bidding. See generally, 47 U.S.C. §§309(j)(3), 309(j)(4)(C) and 309(j)(7).

² 47 U.S.C. §§309(j)(1), 309(j)(2)(A). The commercial license issued to Hye Crest would not be subject to the competitive bidding process under §309(j) since it is an existing license, not an initial license.

The House Report notes that "unless the Commission is sensitive to the need to maintain opportunities for small businesses, competitive bidding could result in a significant increase in concentration in the telecommunications industry." H.R. No. 103-111 at 254. Thus, in issuing licenses for a particular service by competitive bidding, the Commission is required to establish adequate protective measures and effective preferential schemes to fulfill the explicit legislative directive to promote small business, prevent the concentration of licenses, ensure effective competition by disseminating licenses among a wide variety of applicants, and support the development of new technologies for the benefit of the public.

In the LMDS NPRM, the Commission has proposed the allocation of two 1 GHz blocks of spectrum (27.5 -29.5 GHz) per service area, with 1 GHz per licensee, to enable LMDS licensees to have sufficient bandwidth within which to compete with incumbent service providers. For example, coaxial cable used by cable operators has 1 GHz of spectrum capacity. As the record in the LMDS proceeding reflects, LMDS licensees will require a 1 GHz block of spectrum in order to provide a 50 channel competitive video alternative. Only with such an allocation will LMDS be able to fulfill its potential as a viable and immediate high quality, low cost, spectrum efficient alternative to existing cable services throughout the nation.

However, the Commission must be careful that in subjecting this innovative and much needed new service to competitive bidding, it does not

foreclose the opportunity for small entities to acquire licenses. The FCC's Small Business Advisory Committee ("SBAC") has recognized that capital formation is the primary obstacle to market entry by small businesses. As the SBAC has stated:

Acquisition and operation of regulated communications facilities is extremely capital intensive. Without a track record of ownership and substantial capital resources, new entrants typically encounter difficulties obtaining start-up funds.

Report of the FCC Small Business Advisory Committee to the Federal Communications Commission Regarding Gen. Docket 90-314, ("SBAC Report"), September 15, 1993, at 3. Thus, absent sufficient protection in the auction procedures, small and mid-size businesses³ will be effectively precluded from making successful bids to acquire LMDS licenses due to their probable lack of financial resources to out-bid large corporations.⁴ As a result, LMDS licenses will be concentrated among a few, well-financed, Fortune-500 corporations, against the clearly stated will of Congress to promote small business

³ The proposed "small business" definition, the Small Business Administration's \$6 million net worth or the 1,500 employee limit in 13 C.F.R. §121.601, both are grossly unrealistic as discussed in Part II, section 2, *infra*.

⁴ The Commission recently commenced a proceeding to reexamine the pioneer's preference rules. See In the Matter of Review of the Pioneer's Preference Rules, Notice of Proposed Rulemaking, ET Docket No. 93-266 (released October 21, 1993). If the Commission eliminates or amends the pioneer's preference rules, or decides to require payment for pioneer's preference licenses, thus erasing the potential reward to an innovator of a new technology, a small, entrepreneurial innovator such as Suite 12 will be forced to take on a capital intensive "partner" to obtain the finances necessary to bid or otherwise pay for the license. As a result, it is highly likely that the pioneer would lose substantial ownership and control over its innovation.

proliferation -- particularly for services which are local in nature, such as LMDS.⁵ Additionally, the lack of diversity among LMDS licenses will reduce the number of potential video alternatives available to the public and lessen competition in the video services marketplace.

The fact that ownership trends in the telecommunications industry have become more concentrated in larger firms provides further basis for protecting smaller firms.⁶ Accordingly, to ensure that potential LMDS operators of all sizes are given an equal opportunity to acquire licenses in order to compete in providing services to consumers in the video marketplace, the issuance of LMDS licenses through a competitive bidding scheme must include sufficient protection for small businesses. Otherwise, the marketplace will become further concentrated, small business will be precluded from robust participation, competitive services will be diminished, and the deployment of new technologies will be inhibited.

⁵ The House Report notes that "the characteristics of some services are inherently national in scope, and are therefore ill-suited for small business. However, other services are local, and could well provide new opportunities for small business participation." See H.R. Rep. No. 103-111 at 254. Suite 12's system operates on a cell-by-cell basis, allowing the system to deliver programming targeted to the unique demographics of a particular cell -- making the system truly local in nature.

⁶ The SBAC Report notes that in 1991, firms employing less than 249 employees possessed 35.1% of the market, whereas only two years earlier, that figure was as high as 52.5%. See SBAC Report at 3.

2. The "Small Business" Designation Under §309(j) Must Realistically Conform with the Capital-Intensive Telecommunications Industry.

The Budget Act explicitly requires the Commission to ensure that small businesses, rural telcos and businesses owned by minorities and women are "given the opportunity to participate" in the provision of spectrum based services." 47 U.S.C. § 309(j)(4)(D); see Conference Report at 482-484. To accomplish this directive, the Commission has classified certain groups, including small business, as "designated entities" warranting special treatment.

The Commission seeks comment on whether it should rely on the definition of "small business" set forth by the Small Business Administration ("SBA"). As noted by the SBAC, the SBA classifies an entity as "small" and thus worthy of SBA financial assistance if it has a net worth of \$6 million or less, with average net income after Federal income taxes for the preceding two years of \$2 million or less.⁷ Alternatively, the SBA provides that an entity may qualify as "small" if it meets the size standard for its industry as set forth in 13 C.F.R. §121.601 — under this regulation, "radiotelephone communications" businesses having less than 1,500 employees are considered "small."⁸

Both proposed definitions of small business are unrealistic and impractical in terms of the actual makeup of the telecommunications marketplace in the United States today. As the SBAC Report itself notes, the \$6 million

⁷ See NPRM at footnote 51; SBAC Report, at 20.

⁸ Id.

limit might be too low for the capital-intensive telecommunications industry. See SBAC Report at 21. The construction and roll-out costs necessary to provide LMDS to a multi-million person service area strongly suggest that this is indeed the case. The addition prospect of having to absorb an auction price as a necessary predicate to entering the market only exacerbates the capitalization difficulties facing small businesses. If the Commission utilizes the SBA's low figures, it will effectively exclude almost any small business such as Suite 12 from gaining access to the market, directly inconsistent with the explicit Congressional mandate to ensure the ability of small businesses to participate in such services.

Even if the Commission were to increase the net worth element of the SBA definition, this standard, which is based in part on the reporting of net income after taxes, is an ineffective way to determine business size since many large companies report profits based on a variety of factors independent of company size. For example, in connection with the proposed merger of Bell Atlantic and Telecommunications Inc. ("TCI"), the cable and programming giant, it was reported that TCI has never reported a full year profit.⁹ Certainly, a company as large as TCI is not what Congress had in mind when it mandated protection for "small" businesses.

Likewise, the employee cap of 1,500 proposed by the SBA is much too large for a "small" business, and would frustrate explicit Congressional intent by

⁹ See The Washington Post, October 19, 1993, Financial Section, at 3.

permitting many medium and large size businesses to qualify for special treatment as small businesses. Moreover, a numerical employee standard would be extremely difficult to oversee and verify from a regulatory standpoint, and it could be circumvented by the hiring of consultants and sub-contractors.

In order to serve the Congressional goal of promoting small business, the Commission must adopt a realistic definition that is exclusively tied to company revenue in order to encompass that level of small business truly able to compete in the marketplace. Thus, consistent with the legislative intent of Section 309(j), Suite 12 submits that the singular effective measurement of "small" businesses should be those with \$75 million or less in annual sales. Suite 12 believes that this figure, which would be easily ascertainable and verifiable in terms of regulatory efficiency, would allow true "small" businesses in today's communications marketplace to compete with the large vertically and horizontally integrated corporate entities that could easily dominate spectrum auctions involving new and threatening technologies such as Suite 12's CellularVision system.

3. The Commission Should Adopt Preferential Payment Plans for Small Businesses

Additionally, in connection with the need to adopt a realistic definition of small business as discussed above, Suite 12 supports the Commission's proposal to provide preferential payment plans for small businesses to pay for the spectrum they secure by auction. However, Suite 12 proposes that the

Commission allow small businesses who prevail at an auction to pay the amount of the winning bid on an interest-free, installment basis over the life of the license. Payment could be made monthly, or quarterly, at the option of the licensee, beginning in the second year of the license. This plan would allow small businesses to acquire licenses without being crippled financially, while at the same time enhancing their ability to retain the capital sufficient to roll-out their systems and meet the build-out requirements ultimately adopted by the Commission.¹⁰

**4. Incumbent Licensees in Competing Services
Should Be Prohibited from Holding a Controlling
Ownership Interest in any Single LMDS
Applicant or Licensee.**

The Commission goes to great lengths in the NPRM to propose safeguards designed to protect the integrity of the auction process. The laudable rationale behind these proposals seeks to prohibit, among other things, spectrum hoarding and warehousing, and collusion. Suite 12 supports these measures, especially the performance requirements, the anti-trafficking restrictions, and disclosure requirements. However, Suite 12 firmly believes that the Commission

¹⁰ Providing small businesses with such preferential payment options is consistent with the nurturing regulatory treatment afforded to emerging television networks by the Commission in recent years. See generally Evaluation of the Syndication and Financial Rules, First Report and Order, 6 FCC Rcd 3094, as modified, Memorandum Opinion and Order, 7 FCC Rcd 345 (1991); Second Report and Order, 8 FCC Rcd 3283, as modified, Memorandum Opinion and Order, FCC 93-458 (released October 22, 1993).

must do considerably more along these lines if the Congressionally mandated goals of promoting competition through an efficient and robust use of the spectrum are to be achieved.

Suite 12 is troubled, as is the House Report, by the possibility that incumbent service providers who fear the real competition which LMDS portends could win a bid for a license and then either not deliver the service, or do so in a non-competitive manner. For the large, powerful incumbent cable provider, for example, acquiring a license to offer a competing service such as LMDS would essentially give the incumbent cable operator a license to kill the competition which the fledgling LMDS service would otherwise provide.

Accordingly, Suite 12 proposes that the Commission allow incumbent spectrum users in competing services to hold only non-controlling (i.e., 49% or less) interests in LMDS applicants or licensees. For purposes of LMDS, incumbent spectrum users in competing services would consist of cable, broadcast, and telephone licensees. This safeguard would further allay the Commission's concerns about preventing the stockpiling and/or warehousing of licenses. At the same time, it would recognize the realities of the marketplace, and the important role that strategic partnerships can play in bringing financial support and other strategic resources to small competitive businesses such as Suite 12.